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The Minister's Working Group on Education Finance

Final Report

May, 2004

Executive Summary

The Minister's Working Group on Education Finance was created in May 2002 in response to the 2001 Association of Manitoba Municipalities task force report entitled, Rethinking Education Funding Challenges and Opportunities.

The Working Group included representation from school board, municipal and teacher organizations. and staff support resources from various Government departments. The Working Group was mandated to research and to analyze strategies which will reduce Manitoba's reliance on property taxation to fund public education and ultimately, to recommend a detailed strategy to achieve this outcome.

Guiding Principles

The Working Group articulated five key principles to guide its deliberations and the analysis of alternative funding arrangements. These include:

1. that the provision of high quality, universally accessible public education is a cornerstone of a highly developed society promoting both prosperity and good citizenship;

2. that all members of society share responsibility to sustain a high quality public education system;

3. that Government is responsible for establishing the parameters of a defined education program that will provide students with the opportunity to achieve their potential and pursue life goals including post-secondary education and employment;

4. that geographic location or local economic factors cannot be impediments to students' entitlement to a defined education program; and

5. that a level of local autonomy which includes taxing authority is necessary in order to meet local needs as reflected or determined by local communities.

Recommendations

Seven funding models were reviewed, all of which substantially increase the provincial contribution to public school division operating expenditures and all of which reduce property taxation in support of public education.

In coming to its conclusions, the Working Group sought to balance the urgent need for decreased reliance on property taxation revenues to fund public education within the scope of the challenge and the fiscal capacity of the province to act.

The Working group, therefore, recommends:

- adoption and implementation of Model G to effect

- an increase in provincial funding support from the current 57% of divisional operating expenditures to 80%, resources to be derived from provincial general revenues and from taxation levied on farm and non-residential property classes:

- a decrease in school division funding requirement from the current 43% to 20%. 15% to be derived from taxation levied on residential property only and 5% from other revenue sources; and

- an initial overall decrease in property taxation revenues in support of public education from 51% to 37%.

To implement the proposed funding model, the Working Group recommends:

- the pooling of farm and non-residential assessments and taxation of these property classes by the province at uniform mill rates for each;

- establishment of initial uniform mill rates for farm and non-residential property classes at the existing provincial average rate in order that the current total amount of property taxes paid by these two property classes remain unchanged in the first year of implementation;

- a 3-year self-funding phase-in period to effect the transition to uniform mill rates for farm and non-residential assessment pooling;

- a 1% increase in provincial retail sales tax to fund the increased general revenue requirement;

- legislative measures to ensure that property tax savings are passed through from landlords to tenants in rental properties;

- mechanisms to avoid erosion of initial property tax savings to home owners through subsequent increases in school division tax levies to address any mismatch between provincial funding increments and school division cost changes; and

- development of a funding distribution model which closely matches provincial funding to current actual cost factors of program and service delivery in schools.

To ensure long term sustainability of the proposed funding model, the Working Group recommends:

- articulation of a defined education program and provincial funding commensurate to ensure equity of entitlement and access for all K – S4 students in Manitoba;

- development of mechanisms to ensure on-going congruency between labour costs and the level of provincial contribution to divisional operating expenditures;

- annual adjustments to school divisions' operating funding to reflect the actual cost increases incurred in delivery of a defined education program for all students;

- separation of operating and capital funding requirements in determining provincial contribution to maintain 80% operating support;

- sourcing of annual provincial funding increases from general revenues to ensure that over time, farm and non-residential property taxation becomes a diminishing portion of the total revenue base for public education;

- review and revision of existing property taxation structures and mechanisms to address current inequities which have been identified; and

- review of provincial-municipal tax sharing arrangements with Manitoba municipalities.

INTRODUCTION

The Minister's Working Group on Education Finance was formed in May, 2002 in response to a key recommendation from the Association of Manitoba Municipalities (AMM) Task Force Report "Rethinking Education Funding: Challenges and Opportunities" (April 2001).

The Working Group was charged with a mandate

- to research and analyze strategies that may be adopted by the government to reduce Manitoba's reliance on property taxation to support education;

- to recommend a detailed strategy to reduce Manitoba's reliance on property taxation to support education; and

- to provide a comprehensive outline of the implications of the recommended strategy respecting

    - type and level of taxation by government and School divisions,
    - revenue and programming equity of school divisions,
    - governance of school divisions including the impact on collective bargaining, and
    - others as determined by the Working Group.

The Working Group was comprised of elected and administrative representatives at the school board and municipal levels. as well as a representative of the Manitoba Teachers' Society. Participants included:

Grant Buchanan	Chairperson
Glen Anderson	Manitoba Teachers' Society
Jim Dalton	Manitoba Association of School Superintendents to May, 2003
Carolyn Duhamel	Manitoba Association of School Trustees
Guy Lacroix	Manitoba Association of School Superintendents June, 2003 to present
Rick Martel	Association of Manitoba Municipalities
Kevin McKnight	Manitoba Association of School Business Officials
Wally Melnyk	Manitoba Municipal Administrators' Association
Robert Weselowski	City of Winnipeg

Staff support to the Working Group was provided from the provincial ministries of Manitoba Education, Citizenship and Youth, Finance and Intergovernmental Affairs.

Staff persons involved were:

Laurie Davidson	Intergovernmental Affairs
Steve Power	Education, Citizenship and Youth
Steve Watson	Finance

The Working Group recognizes the commitment of individuals and representative organizations who have participated in this effort over the past eighteen months and acknowledges the invaluable support of provincial department personnel in the provision and analysis of data to inform group deliberations and the recommendations contained within this report.

INTERIM STATUS REPORT

In November, 2002, an interim status report was presented to the Minister of Education and Youth outlining the Group's progress to that point and the outstanding work to be completed in this second phase.

The initial discussions of the Working Group were largely exploratory in nature and structured to facilitate better information sharing and work planning. As a beginning point, the Working Group explored values and beliefs of the various organizations regarding public education and identified five key principles to guide its deliberations and the analysis of alternative funding arrangements. These are

1. ***That public education is a public service that benefits all society;***

   The provision of high quality, universally accessible public education is a cornerstone of a highly developed society promoting both prosperity and good citizenship.

2. ***That all members of society are responsible for the public education system;***

   All members of society share responsibility to sustain a high quality public education system.

3. ***That there must be a defined education program;***

   Government is responsible for establishing the parameters of a defined education program that will provide students with the opportunity to achieve their potential and pursue life goals including post-secondary education and employment.

4. ***That all students must have equitable opportunity to access a defined education program; and***

   Geographic location or local economic factors cannot be impediments to students' entitlement to a defined education program.

5. ***That local autonomy is important.***

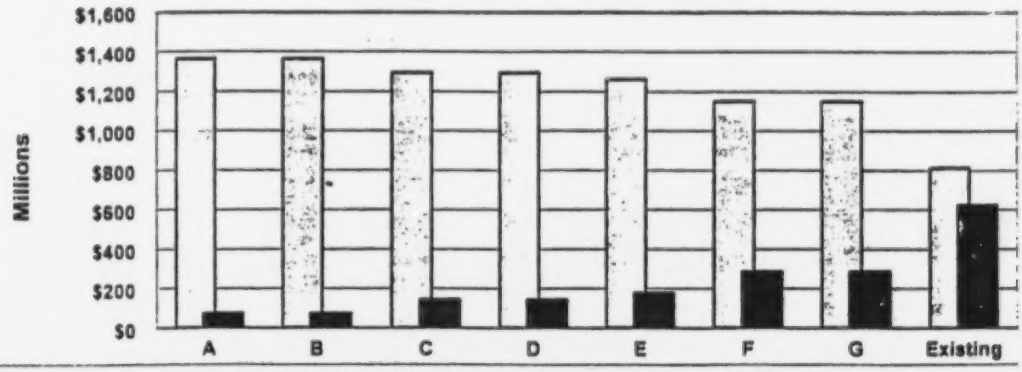
A level of local autonomy that includes taxing authority is necessary in order to meet local needs as reflected or determined by local communities.

Other discussions in Phase 1 included a comparative review of education funding models and trends in Manitoba and other Canadian provinces, an exploration of issues related to municipal and provincial tax competitiveness, and an identification of inequities within Manitoba's current property tax structure. Modeling and analysis of alternative funding structures were identified as the key elements of focus for the second phase of deliberations.

The Working Group examined seven different funding configurations based upon school division operating expenditures of $1.43 billion in the 2003-2004 school year. It should be noted that the Working Group, in its modeling exercise, did not challenge the current level of operating expenditures in school divisions nor did it assume any reductions in the current level of provincial funding to school divisions. Rather, all models anticipate subsequent year increases in provincial funding commensurate with provincial economic growth and any additional costs incurred by school divisions for new program and service mandates resulting from shifts in provincial education policies or directions. In addition, all models also assume that approximately 5% of school divisions' own source revenues will be derived from sources other than property taxation, as is currently the case [1].

The models articulated in this report demonstrate the potential impacts of increasing the total provincial contribution to operating support from its current level of about 57% to 80, 88, 90 and 95 % respectively. Figure 1 illustrates the funding distribution which would result between the province and school divisions for each of the models examined. In Models A and B, school division revenues are entirely derived from our source revenues. In Models C through G, and in current financing arrangements, school division revenues include both own source and property taxation revenues.

Figure 1 - Provincial and School Division Contributions as a Portion of Total Operating Expenditures



	A	B	C	D	E	F	G	Existing
Provincial	$1,363	$1,363	$1,293	$1,293	$1,260	$1,150	$1,150	$815
School Division	$75	$75	$145	$145	$178	$288	$288	$623
% Contribution	95/5	95/5	90/10	90/10	88/12	80/20	80/20	57/43

Note [1]:

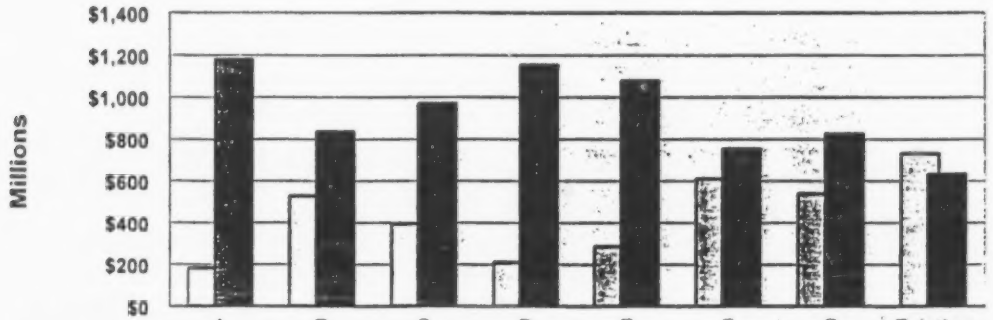
School division own source revenues are derived from two sources - locally levied property taxation (Special Levy) and other source revenues, primarily tuition and transfer fees for out of division students. These other source

revenues constitute approximately 5% of total operating budgets. All models assume that these other source revenues will remain stable into the future at about 5% of divisional operating budgets.

While all models achieve the desired result of reducing reliance on property taxation to fund Manitoba public schools, no single model eliminates property taxation entirely as a funding source for public education. This mirrors long standing practice in Manitoba and existing education funding models in six other Canadian provinces (See Appendix A).

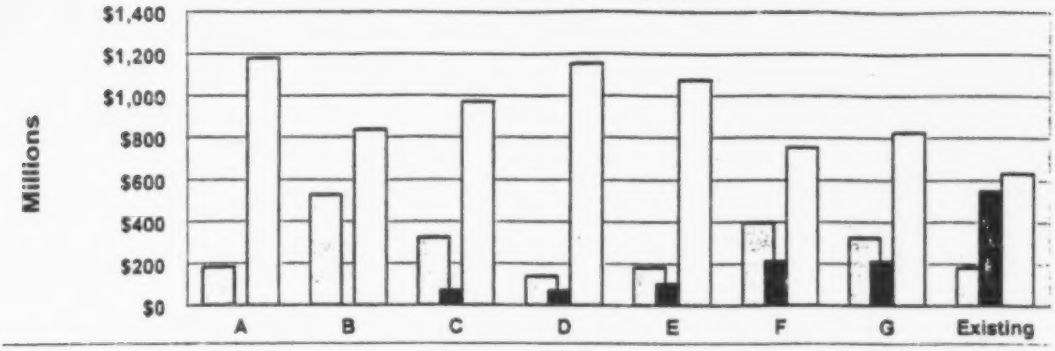
Total property taxation reduction across the seven models ranges from 17% to 75% as illustrated in Figure 2. Figure 3 depicts the breakdown of revenue sources for each model in terms of the provincial Education Support Levy (ESL), divisional Special Levies (SL) and provincial general revenues. Divisional 'own source' revenues at 5% of operating expenditures are additional to the numbers and percentages modeled in Figures 2 and 3.

Figure 2 - Total Property Taxation and General Revenue Contribution by Model



	A	B	C	D	E	F	G	Existing
Property Tax	$183	$528	$394	$210	$286	$610	$538	$731
General Revenue	$1,180	$835	$969	$1,153	$1,077	$753	$825	$632
% Contribution	13/82	37/58	27/67	15/80	20/75	42/52	37/57	51/44

Figure 3 - Education Support Levy, Special Levy and General Revenue Contribution by Model



	A	B	C	D	E	F	G	Existing
ESL	$183	$528	$324	$140	$183	$397	$325	$183
Special	0	0	$70	$70	$103	$213	$213	$548
General Revenue	$1,180	$835	$969	$1,153	$1,077	$753	$825	$632

Note : ESL is the Provincial Education Support Levy
Special is the School Division Special Levy

The discussion which follows outlines, for each model considered, the shifts in property tax incidence, additional general revenue requirements from the provincial treasury, and the property tax reductions which would occur in residential, commercial and farm classes of property. The figures referenced in the discussion of each model are displayed in Table 1.

Table 1 – Comparative summary of public school funding models

2003 Existing Level	Residential	Commercial	Farm	Total	% of total
Education Support Levy	72	111	0	183	13%
Special Levy	334	167	47	548	38%
Property Tax sub total	**406**	**278**	**47**	**731**	**51%**
General Revenue				632	44%
Other own source				75	5%
Total	406	278	47	1,438	100%
Recap:					
Provincial share				815	57%
School division share				623	43%
Total				**1,438**	**100%**

Notes:

*[1] **For presentation purposes, 2003/04 special requirement property tax levels have been used in the model analysis.**

Model A: rebalancing existing property taxes and elimination of special levy, replace with general revenue

Model B: rebalancing existing property taxes and elimination of special levy (take over SL plus general revenue)

Model C: 90% provincial funding with phase out of provincial property tax/School div at 10% (5% property tax, 5% other)

Model D: 90% provincial (80% general revenue/10% ESL farm and commercial/School div at 10% (5% property tax, 5% other)

Model E: 88% provincial funding (ESL 13%/general revenue 74%)/school division at 12% (7% SL and 5% other)

Model F: 80% provincial funding/School div at 20% (15% residential tax, 5% other)

Model G: 80% provincial funding, provincial ESL take over SL farm and commercial/School div at 20% (15% residential tax, 5% other)

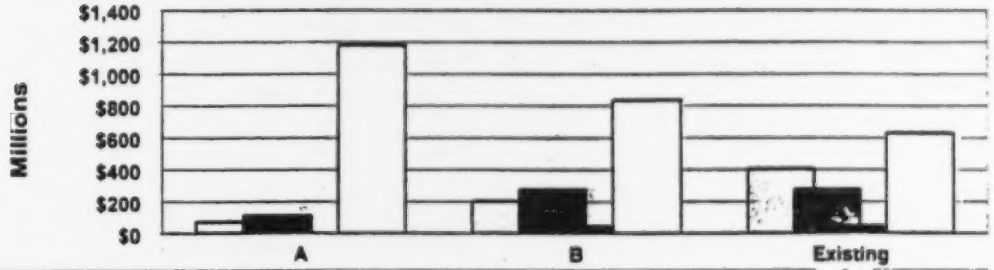
Model	A	B	C	D	E	F	G
Provincial funding	95%	95%	90%	90%	80%	80%	80%
Education Support Levy	$183M	$528M	$324M	$140M	$183M	$397M	$325M
- Residential	no change	+$131M	($72M)	($72M)	no change	no change	($72M)
- Commercial	no change	+$167M	+$167M	}	no change	+$167M	+$167M
- Farm	-	+$47M	+$47M	}+$29M	-	+$47M	+$47M
General Revenue impact	-$465M	+$120M	+$337M	+$521M	+$445M	+$121M	+$193M
Property Tax credit impact	No change	No change	No change	No change	Eliminate ($106M)	No change	No change
Provincial-municipal tax sharing (PMTS)	Eliminate ($83M decrease)	Eliminate ($83M decrease)	No change	No change	No change	No change	No change
School Division property tax	Eliminate ($548M decrease)	Eliminate ($548M decrease)	$70M ($478M decrease)	$70M ($478M decrease)	$103M ($445M decrease)	$213M ($335M decrease)	$213M ($335M decrease)
School Division tax base	None	None	All property	All property	All property	Residential only	Residential only
Total Property Tax Change							
- Residential	($334M)	($203M)	($365M)	($364M)	($268M)	($121M)	($193M)
- Commercial	($167M)	-	+$21M	}	($139M)	-	-
- Farm	($47M)	-	+7M	}($157M	($38M)	-	-
Total	($548M)	($203M)	($337M)	($521M)	($445M)	($121M)	($193M)

Model descriptions

95% provincial contribution models

In models A and B the province funds 95% of divisional operating costs and school division Special Levies (SL) are completely eliminated. In both instances, existing property tax credit programs remain unchanged and Provincial Municipal Tax Sharing (PMTS) dollars of $83M are re-allocated to education. It is assumed that municipalities recoup lost PMTS dollars through local property taxation or other own source revenues.

Figure 4 - 95% Provincial Contribution
Property Taxation and General Revenue Requirement



	A	B	Existing
Residential	$72	$203	$406
Commercial	$111	$278	$278
Farm	$0	$47	47
General Revenue	$1,180	$835	$632

At this point the two models diverge. In Model A, tax dollars lost through elimination of school division Special Levies are replaced by an increased general revenue contribution of $548M ($465M plus $83M re-allotted from PMTS program) and the provincial Education Support Levy (ESL) is carried forward at the 2003 level of $183M. In Model B, the province assumes most of the taxing effort previously carried by school divisions, including farm and commercial levies of $47M and $167M respectively and $131M on residential property. These amounts combined with existing ESL revenues on residential and commercial properties provide for a total ESL contribution of $528M. The expansion of the ESL in this manner reduces the additional general revenue requirement in Model B to $203M, ($120M plus $83M re-allocated from the PMTS program).

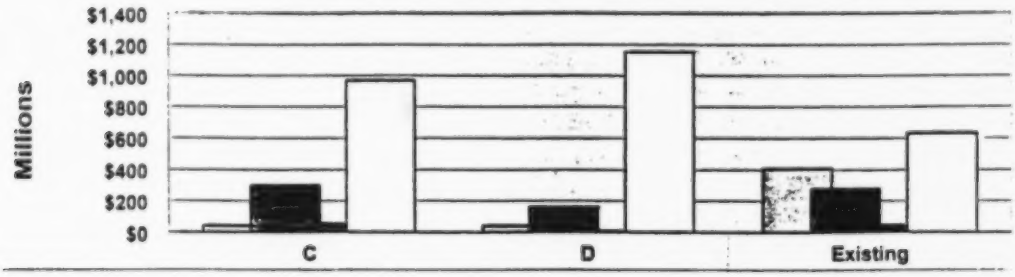
To summarize, the significant differences between Models A and B are property tax reductions - $548M across all property classes in "A" versus $203M on residential only in "B", and resulting additional general revenue requirements of $548M and $203M respectively.

90% provincial contribution models

To raise provincial education funding from its current level to 90%, an additional $478M in revenues would be required from provincial sources. The Working Group examined two funding source options to meet this requirement.

Figure 5 -

90% Provincial Contribution
Property Taxation and General Revenue Requirement



	C	D	Existing
Residential	$42	$42	$406
Commercial	$298	$161	$278
Farm	$54	$7	$47
General Revenue	$969	$1,153	$632

In both Models C and D, property tax credit programs and the existing PMTS program remain intact. In both instances as well, school divisions retain taxing authority across all classes of property raising approximately 10% or $145M of required operating revenues through a combination of property taxation and other source revenues, $70M and $75M respectively.

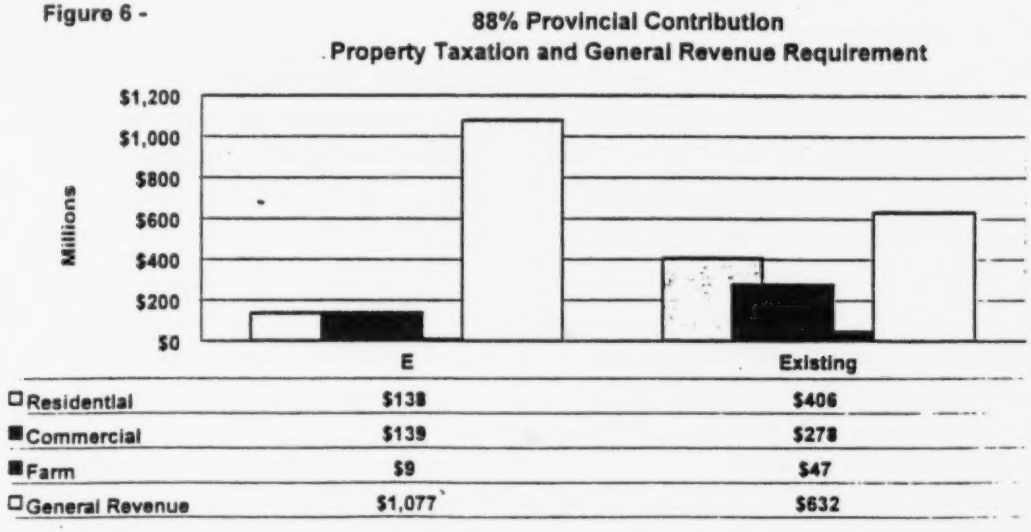
In Model C, the province eliminates ESL on residential properties (-$72M) but assumes existing school division taxation on farm and commercial property at uniform provincial mill rates. The model achieves a significant reduction in total residential property taxation (-$364M) but creates modest increases of $7M and $21M in farm and commercial taxation revenues respectively, owing to a redistributive effect which occurs from residential to farm and commercial property when the school division tax of $70M is levied across all property classes. The resulting additional general revenue requirement in Model C is $337M.

In Model D, the provincial contribution is based upon 10% ($140M) from property taxation on farm and commercial properties and 80% from general revenues. Residential ESL is completely eliminated. In total, residential property taxation declines by $364M and combined farm/commercial taxation by $157M. The resulting additional requirement from provincial general revenues is $521M.

88% provincial contribution model

Model E differs from the others examined in that the 80/20 ratio is based on a consideration of general revenues to total property taxation rather than total provincial contribution relative to school division contribution. In this model, combined provincial and school division property taxation contributes 20% of the required revenues for school division operating budgets. ESL structure is unchanged, taxation revenue on residential and commercial property classes remaining constant at the 2003 level of $183M for about 13% of total funding. School divisions retain minimal taxing powers across all classes of property, generating only about 7% of required operating revenues. The consequent decrease of $445M in the Special Levy breaks down to $268M in residential, $139M in commercial and $38M in farm land taxation reductions. The resulting additional general revenue requirement from provincial sources is $445M.

Figure 6 -



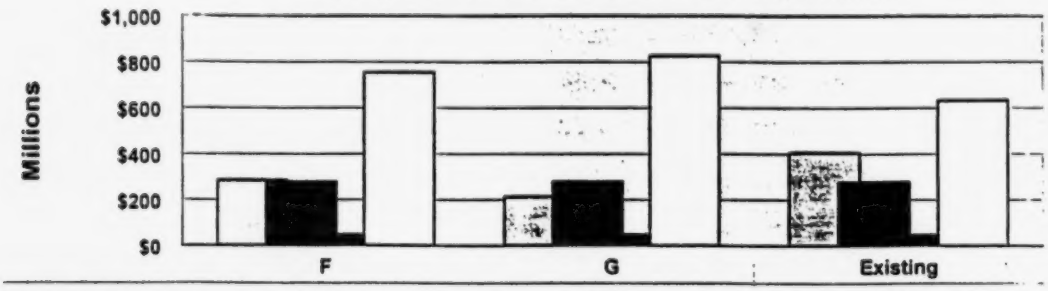
80% provincial contribution models

Models F and G are similar in several important aspects. While neither model impacts existing PMTS or property tax credit programs, both models incorporate the pooling of farm and commercial assessments and the transfer of taxing authority for these property classes from school divisions to the province. In both models, school divisions retain limited taxing authority on residential property.

The significant difference between Models F and G is the structure of the provincial Education Support Levy. In model F, the ESL is applied to all property classes; in contrast, Model G restricts the ESL to farm and commercial property classes only. Property tax reductions in both models impact residential property only, $121M in Model F and $193M in Model G, to be offset in each instance by corresponding increased general revenue contributions.

Figure 7 -

80% Provincial Contribution
Property Taxation and General Revenue Requirement



	F	G	Existing
Residential	$285	$213	$406
Commercial	$278	$278	$278
Farm	$47	$47	$47
General Revenue	$753	$825	$632

Discussion of Alternative Funding Models

In assessing the relative merits of the models outlined above, the Working Group looked first at the guiding principles articulated earlier in this report. These include

1. that public education is a public service that benefits all society;
2. that all members of society are responsible for the public education system;
3. that there must be a defined education program [2];
4. that all students must have equitable opportunity to access defined education programs; and
5. that local autonomy is necessary in order to meet local needs as reflected or determined by communities.

A further consideration included the feasibility of the models in light of current Government resources and priorities.

All models examined increase the provincial contribution to school division operating support quite dramatically from the current 56% to 80% and beyond, and all models require significant additional dollars from provincial general revenues to offset property tax reductions. To this extent, all models are congruent with the first two principles identified by the Working Group. Education funding becomes primarily a provincial responsibility and general revenue contributions drawn on broadly-based revenue streams offset reductions in tax levies applied only to property owners. Basic programming inequities attributable to the relative taxing capacity of individual school divisions can presumably be addressed through Government policy decisions which define program offerings and requirements, and equalization measures in the funding distribution model which take into account the actual cost of program and service delivery in each division.

Note [2]:

While Working Group members were firmly committed to guiding principle #3 - that there must be a defined education program as the foundation for a provincial education funding policy - definition of that program per se falls outside the parameters of this report. Moreover, the issue of equal access to a defined program is complicated by geographic, demographic and economic factors which can only be addressed through a funding allocation policy which is sensitive to these cost variables. While the Working Group discussed some aspects of a revised funding model, considerably more discussion and analysis would be required and this work most appropriately falls within the terms of reference of the Advisory Committee on the Funding of Schools Program. Finally, given the diversity of Manitoba's communities across the province, it is likely that practical realities and community priorities will produce some diversity in programming from one locale to another. Hence, while equity in public education

remains an important priority, absolute and total equity in all circumstances may prove to be a somewhat elusive goal.

These positive aspects aside, each of the models presents significant challenges to be addressed. In Models A and B, where the provincial contribution rises to 95%, the complete elimination of local taxing authority raises serious concerns about the capacity of elected school boards to address the educational priorities of diverse communities across the province beyond the basic requirements of provincial education policy. Model A, which results in property taxation (ESL) on residential and commercial properties only, and the total absence of any tax effort on farm properties also violates the notion that public education is a shared responsibility and a cost to be borne by all residents in all property classes. Further, the proposed elimination of Provincial Municipal Tax Sharing in Models A and B would necessitate either a reconfigured financial arrangement between the province and its municipalities or an acknowledgement that municipalities would likely recoup lost dollars through their respective taxation efforts, thus negating in part, the education property tax reduction.

The very large increased general revenue requirement in Model A, $465M, is likely to be problematic given the pressure on current Government resources. While reduced general revenue requirement of $120M in Model B is deemed by the Working Group to be a more realistic target, the transfer of school division taxation efforts to the province is contrary to stated Government initiatives and policy regarding the reduction in residential ESL and other forms of taxation. Were Government to adopt this scenario notwithstanding, the introduction of uniform mill rates within property classes would create some tax shifting amongst property owners within each class. Additional provincial revenues would be required to offset any increases which individual property holders might incur in this scenario.

Models C and D, representing provincial contributions of 90%, pose some of the same challenges identified in the first two models. School division taxing authority is severely limited, and at 5% of operating budgets is not hugely significant in terms of local responsiveness to constituents and taxpayers. Additional general revenue requirements in both models are quite high, $337M and $521M respectively, and deemed by the Working Group to be unrealistic in light of other pressures which factor into Government's expenditure priorities. In addition, Model C would produce modest increases in both farm and commercial taxation and the introduction of standard ESL mill rates would result in some tax shifting within each property class. To mitigate tax increases which farm and commercial property owners might experience in this scenario, the province would again need to incur some level of additional cost.

Model E maintains the current structure of the Education Support Levy at 2003 contribution levels. The school divisions' Special Levy, while still applied to all property classes is reduced significantly from current contribution levels. This limitation in school division taxing authority may be deemed by some as too restrictive to ensure a meaningful level of local autonomy in responding to community priorities. The model is also problematic in that it contradicts Government's stated commitment to the eventual elimination of the ESL on residential property. Moreover, the additional general revenue requirement of $445M is ambitious and not deemed realistic at this juncture. A further challenge in Model E is the elimination of the Property Tax Credit program. While this is a position advocated by some participating stakeholder groups, the complexities in the tax credit program as currently structured would require a much more detailed study and analysis than could be undertaken by the Working Group at this time.

The last two models examined, F and G, set provincial contributions to school division operating budgets at 80%, with school divisions accessing 15% of operating revenues from local property taxation - the Special Levy - and the remaining 5% from other sources. In Model F, the additional general revenue requirement of $121M is a more realistically achievable target than in other of the models considered. Contrary to the previous model, Model F maintains total farm and commercial taxation at existing levels, albeit transferring farm and commercial taxation from school divisions (SL) to the province (ESL). And while Model F does produce a significant reduction in residential taxation, it does so only at the school division level (SL), maintaining residential taxation at 2003 ESL levels as in the previous instance. This aspect of Model F also contradicts Government's stated commitment to the gradual elimination of the Education Support Levy on residential property.

Model G achieves a significant shift in the balance of provincial and divisional contributions to school division operating budgets while still maintaining a meaningful level of taxing authority for locally elected school boards. The total reduction of $193M in residential property taxation incorporates Government's commitment to elimination of the ESL within this property class. The offsetting additional general revenue requirement of $193M is a more realistic target than that required in several other of the models examined.

The transfer of farm and commercial taxation from school boards to the province in Model G does not provide any immediate reduction of taxation in these classes. However, this transfer and the establishment of uniform mill rates for farm and commercial properties does achieve a greater level of

taxation equity for property owners within each class. Moreover, the pooling of farm and commercial revenues for re-distribution to school divisions through a provincial funding mechanism has the potential to address program and service inequities in schools resulting from the uneven taxation revenue capacity of school divisions under the current funding structure. Finally the transfer of farm and commercial taxation to the province would allow Government over time to adjust its reliance on these revenue sources to fund public education.

RECOMMENDATION

While there was unanimous agreement within the Working Group about the direction of desired change to fund education in Manitoba, there were differing views as to the extent of the change either necessary or advisable. The Working Group recommendation, therefore, represents a balancing of interests amongst participants, taking into account the political and economic contexts for decision-making about education funding in this province.

Based on the preceding examination of the relative strengths and challenges associated with each model, the Working Group favours Model G as the option which represents the most realistic and achievable structure to change the way in which Manitoba funds its public education system, 80% provincial contribution which includes ESL on commercial and farm properties and 20% local contribution comprised of 15% residential property tax levied by school divisions and 5% other revenue sources. In the view of the Working Group, this model offers the following advantages:

(a) a significant increase in the provincial contribution to school division operating revenues;

(b) a meaningful degree of local autonomy for school boards through retention of some taxing authority on residential properties to meet local needs and priorities;

(c) distribution of the tax load across all property classes – residential (school division levies), commercial and farm (provincial levies);

(d) an overall reduction in residential taxation which incorporates Government's stated commitment to elimination of the Education Support Levy on residential property;

(e) more uniform taxation levels across commercial and farm properties through the implementation of a common provincial mill rate, with the opportunity for Government to make further adjustments it deems appropriate to achieve greater levels of educational and taxation equity for all Manitobans;

(f) no impact on other existing programs such as Provincial-Municipal Tax Sharing (PMTS) or property tax credits; and

(g) an additional general revenue requirement more modest and hence likely more achievable than amounts required in several other models.

Implementation of the Recommendation

Implementation of Model G to replace Manitoba's current approach to funding public education would require an increase of $335M in the total provincial contribution to school division operating budgets. Clearly, both the structure and the magnitude of the proposed change present many complexities requiring particular strategies to address tax shifts and mitigation requirements, balance of funding requirements, school funding formula impacts and sustainability issues both short and long term.

Tax shifts and mitigation requirements

Existing school division property tax levels on a school year basis include taxation on commercial and farm property of $214M ($167M and $47M respectively). Transferring tax authority on commercial and farm property from school divisions to the province as proposed in Model G would raise the equivalent amount on those properties through the ESL, thus generating $214M for distribution to school divisions through a new or revised provincial funding formula.

A transfer of taxing authority from school divisions to the province in this manner would accomplish multiple objectives:

- increase the provincial funding base and resulting annual increases for public school funding;
- increase tax equity by removing an inequitably distributed property base from direct school division taxation;
- allow the sharing of the commercial and farm property assessment base to all school divisions through the funding formula;
- result in provincial control of commercial and farm property taxation, thereby allowing the province to respond more directly to different policy objectives in regard to farm and commercial economies;
- provide a greater degree of taxation equity through the application of uniform provincial mill rates for farm and commercial properties; and
- maintain an important linkage between education benefits for all Manitobans in the public education system and sharing the burden across all ratepayers.

In effecting the transfer of taxing authority on farm and commercial property from school divisions to the province, the province would need to establish standard mill rates for farm and commercial property to maintain the existing revenue of $325M from these sources. Because a combined standard mill rate would result in tax shifting between these property classes, it is recommended that a different standard provincial mill rate be applied to each property class. Averaging effects will then produce tax shifting within property classes, rather than between farm and commercial property class.

Presently, commercial property is taxed at variable mill rates ranging from a low of 33.6 mills in Evergreen School Division (17.1 mills SL + 16.5 mills ESL) to a high of 50.3 mills in Mystery Lake School Division (33.8 mills SL + 16.5 mills ESL). The average special levy (SL) mill rate on commercial property is 23.6 mills. This rate applied to all commercial property generates $167M. The ESL rate of 16.5 mills generates $111M. Taken together (23.6 + 16.5), these rates produce a standard mill rate of approximately 41 mills which raises, in total, $278M. While total provincial tax load on commercial property will be equivalent to the current total of ESL and SL taxation in this property class, tax on commercial property in low mill rate divisions (primarily rural) will increase while tax on commercial property in high mill rate divisions (primarily urban) will decrease. This is because present urban mill rates tend to be higher than rural mill rates. Therefore, establishing standard mill rates on commercial property will result in a tax shift from urban commercial property to rural commercial property. Across Manitoba school divisions, 7 would experience decreases in commercial taxation mill rates and 28 would experience increases.

- Currently, farm property is taxed at variable school division mill rates ranging from a low of 17.1 mills in Evergreen School Division to a high of 28.6 mills in Winnipeg School Division. A standard mill rate for farm property of approximately 21 mills (average special levy) would be required to raise the same $47M presently raised by school divisions.

A standard mill rate on farm property will result in tax shifts primarily between rural farm properties. As with commercial property, using an average mill rate applied to farm properties to raise the same amount of tax as is currently the case, means that present low mill rate divisions will increase and high mill rate divisions will decrease. In this instance, the farm taxation mill rate decreases in 22 school divisions and increases in 13. Table 2 illustrates the impact of standard provincial mill rates for farm and commercial property.

Table 2

Standard Provincial Mill Rates for Farm and Commercial Property Classes

	Commercial				Farm			
	SL plus ESL ($271M)	Blended Average ($271M)	Change mills	Change %	SL (no ESL) ($45M)	Blended Average ($45M)	Change mills	Change %
Beautiful Plains	34.2	40.1	6.0	17.5%	17.7	20.5	2.8	16.0%
Border Land	37.6	40.1	2.5	6.7%	21.1	20.5	-0.6	-2.9%
Brandon	34.1	40.1	6.0	17.7%	17.6	20.5	2.9	16.5%
Evergreen	33.6	40.1	6.5	19.4%	17.1	20.5	3.4	19.8%
Flin Flon	40.7	40.1	-0.6	-1.5%	24.2	20.5	-3.7	-15.4%
Fort La Bosse	35.7	40.1	4.4	12.3%	19.2	20.5	1.3	6.5%
Frontier	40.1	40.1	0.0	0.0%	23.6	20.5	-3.1	-13.3%
Garden Valley	34.9	40.1	5.2	14.8%	18.4	20.5	2.0	11.1%
Hanover	33.9	40.1	6.2	18.4%	17.4	20.5	3.1	17.8%
Interlake	37.0	40.1	3.1	8.4%	20.5	20.5	0.0	0.0%
Kelsey	39.5	40.1	0.6	1.6%	23.0	20.5	-2.5	-10.9%
Lakeshore	38.4	40.1	1.8	4.6%	21.9	20.5	-1.4	-6.3%
Lord Selkirk	36.7	40.1	3.4	9.3%	20.2	20.5	0.3	1.3%
Louis Riel	40.4	40.1	-0.3	-0.6%	23.9	20.5	-3.4	-14.2%
Mountain View	38.8	40.1	1.3	3.4%	22.3	20.5	-1.8	-8.1%
Mystery Lake	50.3	40.1	-10.2	-20.3%	33.8	20.5	-13.4	-39.5%
Park West	36.1	40.1	4.0	11.0%	19.6	20.5	0.8	4.3%
Pembina Trails	40.9	40.1	-0.7	-1.8%	24.4	20.5	-3.9	-15.9%
Pine Creek	38.2	40.1	1.9	5.0%	21.7	20.5	-1.2	-5.6%
Portage La Prairie	35.0	40.1	5.1	14.5%	18.5	20.5	2.0	10.6%
Prairie Rose	35.7	40.1	4.4	12.4%	19.2	20.5	1.3	6.7%
Prairie Spirit	38.4	40.1	1.7	4.5%	21.9	20.5	-1.4	-6.5%
Red River Valley	37.7	40.1	2.4	6.3%	21.2	20.5	-0.7	-3.5%
River East Transcona	40.5	40.1	-0.4	-1.0%	24.0	20.5	-3.6	-14.8%
Rolling River	37.2	40.1	2.9	7.8%	20.7	20.5	-0.2	-1.2%
Seine River	40.1	40.1	0.0	0.0%	23.6	20.5	-3.1	-13.1%
Seven Oaks	44.8	40.1	-4.7	-10.4%	28.3	20.5	-7.8	-27.6%
Southwest Horizon	36.8	40.1	3.3	9.1%	20.3	20.5	0.2	1.1%
St. James-Assiniboia	36.3	40.1	3.8	10.4%	19.8	20.5	0.7	3.3%
Sunrise	39.1	40.1	1.0	2.6%	22.6	20.5	-2.1	-9.3%
Swan Valley	40.0	40.1	0.1	0.3%	23.5	20.5	-3.0	-12.9%
Turtle Mountain	37.2	40.1	2.9	7.8%	20.7	20.5	-0.2	-1.1%
Turtle River	39.6	40.1	0.5	1.4%	23.1	20.5	-2.6	-11.2%
Western	37.9	40.1	2.3	6.0%	21.4	20.5	-0.9	-4.1%
Winnipeg	45.1	40.1	-5.0	-11.0%	28.6	20.5	-8.1	-28.3%

Notes:

1. **Separate mill rates are required for commercial and farm so as not to shift commercial property tax burden to farm property.**
2. **2003 mill rates are derived for those divisions with differential mill rates.**

These tax shifts on commercial and farm property could be mitigated in two ways. One alternative is to establish standard mill rates at the lowest present common denominator based on Evergreen School Division currently at 17.1 mills. A commercial mill rate of 33.6 mills (17.1 mills + 16.5 mills) and a farm mill rate of 17.1 mills would ensure there would be no tax increases. However, these mill rates would produce a 17% revenue reduction, some $53M, which would have to be offset from some other revenue source, likely general revenues. Ratepayers in present high mill rate divisions could experience substantial reductions in property tax while those in low mill rate divisions like Evergreen School Division would accrue little to no benefit in this approach.

A second approach would involve phasing in mill rate changes, both increases and decreases, over a period of time so that taxpayers have time to adjust to new rates. This would require the maintenance of differential mill rates for a time period of two or possibly three years while mill rates harmonize to the standard mill rates. No additional general revenue contribution would be necessary and at the end of the harmonization period, all farm and commercial property would be taxed at the same average tax rate. During the phase-in period, property tax changes would vary from a tax increase for present low mill rate ratepayers of up to 19.8% for Evergreen School Division ratepayers, to tax decreases of up to 11% in the Winnipeg School Division. Tables 3.1 and 3.2 demonstrate the impact of such a phase-in strategy.

Property tax increases will be difficult to defend to commercial and farm ratepayers who believe that the present lower than average tax rates are already too high. The province could manage this criticism by phasing in a lower than average standard rate as resources permit thereby providing some property tax relief in total to the commercial and farm property class. The province could also choose to freeze commercial and farm property mill rates so there is no further increase in the education tax burden on commercial and farm property.

Table 3.1
Standard Farm Mill Rate Phase-In

School Division	FARM MILLRATE									
					Mill Change from Original			% Change from Original		
	Original	Phase 1	Phase 2	Phase 3	Phase 1	Phase 2	Phase 3	Phase 1	Phase 2	Phase 3
Beautiful Plains	17.6	18.6	19.5	20.5	0.9	1.9	2.8	5.4%	10.7%	16.1%
Border Land	21.1	20.9	20.7	20.5	-0.2	-0.4	-0.6	-1.0%	-1.9%	-2.9%
Brandon	17.6	18.5	19.5	20.5	1.0	1.9	2.9	5.5%	11.0%	16.5%
D.S.F.M.										
Evergreen	17.1	18.2	19.4	20.5	1.1	2.3	3.4	6.6%	13.2%	19.8%
Flin Flon	24.2	23.0	21.7	20.5	-1.2	-2.5	-3.7	-5.1%	-10.3%	-15.4%
Fort La Bosse	19.2	19.6	20.1	20.5	0.4	0.8	1.3	2.2%	4.3%	6.5%
Frontier	23.8	22.7	21.6	20.5	-1.1	-2.2	-3.3	-4.6%	-9.3%	-13.9%
Garden Valley	18.4	19.1	19.8	20.5	0.7	1.4	2.0	3.7%	7.4%	11.1%
Hanover	17.4	18.4	19.4	20.5	1.0	2.1	3.1	5.9%	11.9%	17.8%
Interlake	20.5	20.5	20.5	20.5	0.0	0.0	0.0	0.0%	-0.1%	-0.1%
Kelsey	23.0	22.2	21.3	20.5	-0.8	-1.7	-2.5	-3.6%	-7.3%	-10.9%
Lakeshore	21.9	21.4	20.9	20.5	-0.5	-0.9	-1.4	-2.1%	-4.2%	-6.3%
Lord Selkirk	20.2	20.3	20.4	20.5	0.1	0.2	0.3	0.4%	0.9%	1.3%
Louis Riel	23.9	22.7	21.6	20.5	-1.1	-2.3	-3.4	-4.7%	-9.5%	-14.2%
Mountain View	22.3	21.7	21.1	20.5	-0.6	-1.2	-1.8	-2.7%	-5.4%	-8.1%
Mystery Lake	33.8	29.4	24.9	20.5	-4.5	-8.9	-13.4	-13.2%	-26.3%	-39.5%
Park West	19.6	19.9	20.2	20.5	0.3	0.6	0.8	1.4%	2.9%	4.3%
Pembina Trails	24.3	23.1	21.8	20.5	-1.3	-2.6	-3.9	-5.3%	-10.6%	-15.9%
Pine Creek	21.7	21.3	20.9	20.5	-0.4	-0.8	-1.2	-1.9%	-3.7%	-5.6%
Portage La Prairie	18.5	19.2	19.8	20.5	0.7	1.3	2.0	3.5%	7.1%	10.6%
Prairie Rose	19.2	19.6	20.0	20.5	0.4	0.9	1.3	2.2%	4.5%	6.7%
Prairie Spirit	21.9	21.4	21.0	20.5	-0.5	-0.9	-1.4	-2.2%	-4.3%	-6.5%
Red River Valley	21.2	21.0	20.7	20.5	-0.2	-0.5	-0.7	-1.2%	-2.3%	-3.5%
River East Transcona	24.0	22.8	21.7	20.5	-1.2	-2.4	-3.6	-4.9%	-9.9%	-14.8%
Rolling River	20.7	20.6	20.6	20.5	-0.1	-0.2	-0.2	-0.4%	-0.8%	-1.2%
Seine River	23.6	22.5	21.5	20.5	-1.0	-2.1	-3.1	-4.4%	-8.7%	-13.1%
Seven Oaks	28.3	25.7	23.1	20.5	-2.6	-5.2	-7.8	-9.2%	-18.4%	-27.6%
Southwest Horizon	20.3	20.3	20.4	20.5	0.1	0.1	0.2	0.4%	0.7%	1.1%
St. James-Assiniboia	19.8	20.0	20.3	20.5	0.2	0.4	0.6	1.1%	2.2%	3.3%
Sunrise	22.6	21.9	21.2	20.5	-0.7	-1.4	-2.1	-3.1%	-6.2%	-9.3%
Swan Valley	23.5	22.5	21.5	20.5	-1.0	-2.0	-3.0	-4.3%	-8.6%	-12.9%
Turtle Mountain	20.7	20.6	20.6	20.5	-0.1	-0.1	-0.2	-0.4%	-0.7%	-1.1%
Turtle River	23.1	22.2	21.3	20.5	-0.9	-1.7	-2.6	-3.7%	-7.5%	-11.2%
Western	21.4	21.1	20.8	20.5	-0.3	-0.6	-0.9	-1.4%	-2.7%	-4.1%
Winnipeg	28.6	25.9	23.2	20.5	-2.7	-5.4	-8.1	-9.4%	-18.9%	-28.3%
Provincial Average	**20.5**	**20.5**	**20.5**	**20.5**						

Table 3.2
Standard Commercial Mill Rate Phase-In

School Division	COMMERCIAL MILLRATE									
					Mill Change from Original			% Change from Original		
	Original	Phase 1	Phase 2	Phase 3	Phase 1	Phase 2	Phase 3	Phase 1	Phase 2	Phase 3
Beautiful Plains	34.1	36.1	38.1	40.1	2.0	4.0	6.0	5.8%	11.6%	17.5%
Border Land	37.6	38.4	39.3	40.1	0.8	1.7	2.5	2.2%	4.5%	6.7%
Brandon	34.1	36.1	38.1	40.1	2.0	4.0	6.0	5.9%	11.8%	17.7%
D.S.F.M.										
Evergreen	33.6	35.8	37.9	40.1	2.2	4.3	6.5	6.5%	12.9%	19.4%
Flin Flon	40.7	40.5	40.3	40.1	-0.2	-0.4	-0.6	-0.5%	-1.0%	-1.5%
Fort La Bosse	35.7	37.2	38.6	40.1	1.5	2.9	4.4	4.1%	8.2%	12.3%
Frontier	40.3	40.2	40.2	40.1	-0.1	-0.1	-0.2	-0.1%	-0.3%	-0.4%
Garden Valley	34.9	36.7	38.4	40.1	1.7	3.4	5.2	4.9%	9.9%	14.8%
Hanover	33.9	36.0	38.0	40.1	2.1	4.2	6.2	6.1%	12.3%	18.4%
Interlake	37.0	38.0	39.1	40.1	1.0	2.1	3.1	2.8%	5.6%	8.4%
Kelsey	39.5	39.7	39.9	40.1	0.2	0.4	0.6	0.5%	1.1%	1.6%
Lakeshore	38.4	38.9	39.5	40.1	0.6	1.2	1.7	1.5%	3.0%	4.3%
Lord Selkirk	36.7	37.8	39.0	40.1	1.1	2.3	3.4	3.1%	6.2%	9.3%
Louis Riel	40.4	40.3	40.2	40.1	-0.1	-0.2	-0.3	-0.2%	-0.4%	-0.6%
Mountain View	38.8	39.2	39.7	40.1	0.4	0.9	1.3	1.1%	2.3%	3.4%
Mystery Lake	50.3	46.9	43.5	40.1	-3.4	-6.8	-10.2	-6.8%	-13.5%	-20.3%
Park West	36.1	37.5	38.8	40.1	1.3	2.6	4.0	3.7%	7.3%	11.0%
Pembina Trails	40.8	40.6	40.4	40.1	-0.2	-0.5	-0.7	-0.6%	-1.2%	-1.8%
Pine Creek	38.2	38.8	39.5	40.1	0.6	1.3	1.9	1.7%	3.3%	5.0%
Portage La Prairie	35.0	36.7	38.4	40.1	1.7	3.4	5.1	4.8%	9.7%	14.5%
Prairie Rose	35.7	37.2	38.6	40.1	1.5	2.9	4.4	4.1%	8.3%	12.4%
Prairie Spirit	38.4	39.0	39.5	40.1	0.6	1.1	1.7	1.5%	3.0%	4.4%
Red River Valley	37.7	38.5	39.3	40.1	0.8	1.6	2.4	2.1%	4.2%	6.3%
River East Transcona	40.5	40.4	40.3	40.1	-0.1	-0.3	-0.4	-0.3%	-0.7%	-1.0%
Rolling River	37.2	38.2	39.1	40.1	1.0	1.9	2.9	2.6%	5.2%	7.8%
Seine River	40.1	40.1	40.1	40.1	0.0	0.0	0.0	0.0%	0.1%	0.1%
Seven Oaks	44.8	43.2	41.7	40.1	-1.6	-3.1	-4.7	-3.5%	-6.9%	-10.4%
Southwest Horizon	36.8	37.9	39.0	40.1	1.1	2.2	3.4	3.0%	6.1%	9.1%
St. James-Assiniboia	36.3	37.6	38.9	40.1	1.3	2.5	3.8	3.5%	6.9%	10.4%
Sunrise	39.1	39.4	39.8	40.1	0.3	0.7	1.0	0.9%	1.7%	2.6%
Swan Valley	40.0	40.0	40.1	40.1	0.0	0.1	0.1	0.1%	0.2%	0.3%
Turtle Mountain	37.2	38.2	39.1	40.1	1.0	1.9	2.9	2.6%	5.2%	7.8%
Turtle River	39.6	39.8	39.9	40.1	0.2	0.4	0.5	0.5%	0.9%	1.4%
Western	37.9	38.6	39.4	40.1	0.8	1.5	2.3	2.0%	4.0%	6.0%
Winnipeg	45.1	43.4	41.8	40.1	-1.6	-3.3	-4.9	-3.7%	-7.3%	-11.0%
Provincial Average	**40.1**	**40.1**	**40.1**	**40.1**						

Balance of funding requirements

With school division levies on residential property restricted to 15% of operating budgets and a general revenue increase of $121M from the provincial treasury, home owners would realize, on average, a 36% reduction in Special Levy Taxation. The savings to a home valued at $100,000 at the present average mill rate of 23 mills would be approximately 9 mills or $405. The actual decrease by school division will depend on the funding formula distribution mechanism and the impact of local cost increases beyond future provincial funding levels. When the elimination of residential ESL is included, the total property tax saving to homeowners is approximately 48% over existing education taxation levels.

With $214M raised through the provincial Education Support Levy on commercial and farm property, the remaining requirement of $193M ($121M + $72M required to offset elimination of residential ESL) to reach an 80% contribution level would be sourced through a 1% sales tax increase[3]. A 1% increase in sales tax raises approximately $160M. Assuming that the province, in its previous commitment to the elimination of the residential ESL, has identified a fiscal ability to manage the $72M requirement, the difference of $39M ($160M-$121M) could be directed toward tax mitigation for farm and commercial property.

Regarding the proposed 1% increase in sales tax, there are a number of potential implications and questions to be considered.

- First, for residential ratepayers, it will be important to ensure that any increase in provincial sales tax be offset by the achieved reduction in property taxation. Table 4 provides an analysis of the anticipated impacts for selected family types and income levels within the city of Winnipeg. Based on this modeling, it would appear that most Winnipeg families would realize a net reduction in combined property and sales taxes in this scenario.

Note [3]:

Consumption taxes are generally deemed by economists and tax experts to be a more progressive tax than property tax. For a detailed discussion of this issue, see Allan, Dr. John. University of Regina Restructuring the Funding of K-12 Education in Saskatchewan. Prepared on behalf of the Commission on Financing K-12 Education. Regina 2003.

Table 4

COMPARISON OF A 1% SALES TAX INCREASE WITH A 10 MILL PROPERTY TAX DECREASE - SELECTED FAMILY TYPES

Single person, $30,000, renter

	Old	New	Change
Sales tax	370	423	53
Property Tax	610	483	(126)
Total	980	906	(73)

Single parent, $30,000, renter

	Old	New	Change
Sales tax	481	550	69
Property Tax	774	614	(160)
Total	1,255	1,164	(91)

1-earner family of 4, $40,000, townhouse

	Old	New	Change
Sales tax	943	1,078	135
Property Tax	2,160	1,795	(365)
Total	3,103	2,872	(231)

1-earner family of 4, $60,000, townhouse

	Old	New	Change
Sales tax	1,304	1,490	186
Property Tax	3,810	3,166	(644)
Total	5,114	4,656	(458)

2-earner family of 4, $60,000, standard 2-storey

	Old	New	Change
Sales tax	1,304	1,490	186
Property Tax	3,810	3,166	(644)
Total	5,114	4,656	(458)

2-earner family of 5, $75,000, standard 2-storey

	Old	New	Change
Sales tax	1,741	1,990	249
Property Tax	3,810	3,166	(644)
Total	5,551	5,156	(396)

2-earner family of 4, $100,000, executive 2-storey

	Old	New	Change
Sales tax	2,455	2,806	351
Property Tax	4,935	4,100	(835)
Total	7,390	6,906	(484)

2-earner family of 4, $140,000, executive 2-storey

	Old	New	Change
Sales tax	3,593	4,106	513
Property Tax	4,935	4,100	(835)
Total	8,528	8,206	(321)

Assumptions:

1. Assumes a 10-mill decrease in school division special levy on residential property. Actual effect would depend on the distribution of the incremental provincial revenue through the funding formula. In the projected funding model, mill rate changes in Winnipeg range from a decrease of 4 mills in St. James to a decrease of 11.9 mills in Seven Oaks (see Table 7).
2. The effect on tenants assumes landlords will pass on school tax savings through lowered rent. Without legislative measures to force the savings through, projected tenant savings are not likely which would result in negative impacts on tenants.
3. These examples are for Winnipeg residents. Lower assessed values in rural Manitoba will result in lower property tax savings, without a corresponding reduction in increased sales tax payments. This analysis cannot be replicated for rural Manitoba ratepayers.

Special consideration will also be required to ensure that non-property owners also realize some net benefit in this trade-off of increased sales tax to reduce property taxation revenues in Support of education. Unless landlords as property owners pass on property tax savings through lowered rental rates, tenants would not likely see any cost reductions in this model. Legislative measures will be required to ensure that savings are passed through from landlords to tenants in rental properties.

The proposed 1% increase in retail sales tax must also be examined in terms of its potential impact on Manitoba's inter-provincial competitiveness with Canadian provinces, and particularly with its nearest neighbours. There are three approaches to sales taxes among provinces: Alberta has no such tax. Quebec and three of the Atlantic provinces have a value-added tax that is harmonized with the federal GST, and all other remaining provinces, including Manitoba and its nearest neighbours, have a conventional retail sales tax.

Table 5 – Provincial Sales Tax Rates

Retail Sales Tax Rates (%)

BC	AB	SK	MB	ON	PE
7.5	--	6.0	7.0	8.0	10.0

Harmonized Sales Tax Rates (%)

QC	NB	NS	NF
7.5	8.0	8.0	8.0

A one-point increase in Manitoba's RST, rate would not have a major impact on competitiveness from the point of view of households. At 8%, Manitoba's rate would be equal to that in Ontario, and two point higher than in Saskatchewan.

The more important competitive issue for Manitoba is the impact of a retail sales tax increase on business. In Manitoba, an estimated 40% of RST revenue is derived from business imports, and business in this province is heavily weighted to exports. In provinces where a value-added tax (VAT) is harmonized with the federal GST, no tax is levied on products exported from the jurisdiction; rather, it is

wholly offset by input tax credits. In contrast, under a conventional RST structure, a certain amount of sales tax applied to intermediate inputs is build into the final purchase price of the product. Other things being equal, producers in an RST province like Manitoba, are at a disadvantage when competing for sales against a producer from HST provinces of Quebec, Nova Scotia, New Brunswick and Newfoundland.

Manitoba finance maintains a Manufacturing Competitiveness Model which is used to assess the taxes and costs facing manufacturers in Winnipeg and Brandon as compared to 11 other cities in Canada and the U.S. The model shows that a one-point RST increase would reduce Manitoba's ranking on internal rate of return for a small manufacturer from 4th to 5th out of 13. For a larger manufacturer, the ranking would fall from 5th to 7th.

Table 6 – Competitiveness rankings on 13 Canadian and US cities

Large Manufacturing Firm		
	Base Case Scenario	**1% Increase in Sales Tax**
Pre-Tax Net Income	2	3
After-Tax Net Income	4	5
Internal Rate of Return	5	7
1=highest		
Effective Tax Rate	6	8
Start-up Costs	7	9
1=lowest		

Small Manufacturing Firm		
	Base Case Scenario	**1% Increase in Sales Tax**
Pre-Tax Net Income	2	3
After-Tax Net Income	3	5
Internal Rate of Return	4	5
1=highest		
Effective Tax Rate	5	6
Start-up Costs	7	8
1=lowest		

A further important consideration with regard to any increase in Manitoba's retail sales tax rate is its congruency with provincial balanced budget legislation. Manitoba's *Balanced Budget, Debt Repayment and Taxpayer Accountability Act* requires that a proposed increase in the rate of tax levied under *The Retail Sales Tax Act* and Part 1 of *The Revenue Act* shall first be authorized by the voters in a referendum. There are two exceptions. The first relates to changes to offset changes in federal tax laws, or to restructure the division of tax authority between the federal and provincial governments. The second exception applied to

> "a bill to increase the rate of tax if, in the opinion of the minister, the proposed change is designed to restructure the tax burden and does not result in an increase in revenue."

The act defines "revenue" to be "revenue as reported in the audited financial statements of the operating fund." The Act does not define "tax burden."

In general terms, a case can be made that offsetting changes to sales taxes and Special Levies would not increase the tax burden on Manitobans and therefore would not require approval in a referendum. In contrast, a case can also be made that Special Levies are not revenue as defined under the Act because they do not accrue to the operating fund of the Province. Therefore, a reduction in Special Levies cannot offset an increase in sales tax, within the meaning of the Act.

Under the Act, the opinion of the Minister of Finance is sufficient to determine whether tax changes do or do not result in an increase in revenue. The minister might argue that since school divisions which collect Special Levies are creatures of the Province and given the proposed reduction in a property taxation to offset the increase in retail sales tax, the proposed changes constitute a shift in the tax base rather than any real increase of the tax burden. Consequently, no referendum would be necessary.

In this regard, if an increase in sales tax is offset initially by a reduction in Special Levies, and there is no legal constraint on the ability of school divisions to increase Special Levies subsequently, then the substitution has the practical effect of breaching the restraint on tax rate increases. It might therefore be argued, that the proposed substitution of sales tax revenues to replace property tax revenues would be consistent with the spirit and intent of the Act only if, as in the case for other tax rates, there were to be a referendum requirement applied to any proposed increases in Special Levy mill rates.

Finally, the success the proposed funding structure and its component parts will necessitate steps to ensure that the $121M in additional general revenues flows directly to reduce mill rates. A change of this magnitude will require broad public acceptance that a real benefit will be achieved through lower school division property taxes. Consequently, it will be important to implement measures to avoid a dilution of the property tax savings through increases in school division taxation to address any mismatch in provincial funding increments and school division cost changes.

Ultimately the impact on ratepayers will depend upon the funding formula distribution at the 80% provincial level. At an 80% level it will be more important that funding be closely matched to cost factors. The province will need to establish realistic funding increments that reflect the real increase in school division operating costs, particularly with regard to collective agreements. Even with an accurate cost model it is possible that increased provincial funding share may require some high expenditure divisions to reduce costs while allowing some low expenditure divisions to increase costs. Should this occur, it could potentially result in some greater level of program and/or service equity across divisions.

School funding formula impacts

At the present provincial operating share of 57%, the Funding of Schools Program (FSP) formula variables do not have to be fully linked to the actual cost of program delivery in order to distribute provincial funding equitably. At the 80% level, it becomes critical that FSP grant variables be more fully linked to the actual cost of program delivery to ensure that resources are distributed equitably.

This is particularly important because of the redistribution effect of present farm and commercial property tax levels that would occur in this model. Many rural school divisions are dependent on large farm property tax bases and have a much smaller tax base when only residential property is considered. Similarly, a number of urban school divisions are dependent on a large commercial property tax base. Removal of direct access to these tax bases could result in very significant revenue decreases in some school divisions.

In order to ensure that all divisions are able to maintain existing service levels which have been structured around the financial resources available from the existing property tax base, it will be important to develop FSP variables that return a sufficient level of funding to individual divisions. FSP funding rates and categorical grants will need to more closely approximate actual per pupil costs for basic classroom instruction and for important service areas such as special needs and transportation where service incidence varies among divisions. It may also be necessary to introduce a new formula variable for salary levels in the FSP to recognize wage variances among school divisions that would be difficult to manage with a smaller residential property tax base.

Another important consideration will be the introduction of mechanisms to smooth the tendency of average funding rates at the 80% level to force an increase in costs in present low cost divisions and a decrease in costs in present high cost divisions. The equalization of the residential property base in the FSP will be another important requirement so that low assessment divisions can maintain reasonable tax levels relative to high assessment divisions.

Changes required to the FSP at an 80% funding level require careful study and consultation with stakeholders to develop formula variables that will allow an equitable distribution of provincial funding, both at the revised level and on an ongoing annual basis.

For presentation and discussion purposes, and to evaluate the impact of increased provincial funding at an 80% level, the Working Group requested the Schools Finance Branch to develop modifications to the present FSP to distribute the new 80% funding level. Possible changes to funding formula allocations are illustrated in Table 7. Table 8 demonstrates the impact of these changes as a percentage of divisional operating budgets in an 80% provincial funding model and Table 9 displays how current divisional mill rates would shift in this proposed funding and allocation structure.

Table 7
80% Funding Model - Key Variables

Summary

Based on 2003/04	$ million
Present provincial funding formula level and other provincial revenues	$815
- Assume school division farm and commercial property taxes	214
- General revenue increase	121
Total revised provincial funding formula level	$1,150
Total school division operating revenue (rounded)	$1,438
Provincial percentage ($1,150/$1,438)	80%

Funding formula variable changes

	From	To	$ million
Instructional Support	$1,785	$2,886	$192.5
Level I	$265	$290	$4.4
Level II	$8,780	$15,000	$17.9
Level III	$19,530	$30,000	$11.9
Coordinator clinician	$70/$95/$5	$105/$10/$50	$5.9
Library	$90	$112	$3.3
Professional development	$34	$54	$2.5
Counselling and Guidance	$82	$162	$8.0
Transportation	$255/$375/ $460/$2,675	$400/$400/ $550/$3,000	$3.2
Occupancy	68%/capped	80%/no cap	$46.0
Students At Risk	20% - $10	20% - $50 table rates ↑ $5	$6.0
Enrolment Change	$1,785	$2,886	$2.2
Remoteness Allowance	$550	$600	$0.5
Reduction to Base & Categorical			($0.3)
Higher salary differential *	No	Formula	$57.6
Equalization - threshold mill rate	No	10 mills	($29.2)

* The dollar amount reflects modeling with regard to teachers' salaries only. More detailed analysis and modeling will be required to expand this element of the funding formula to include salary costs for all school division personnel.

Table 8
2003/2004 Funding as a Percentage of Operating Budget

	2003/04 Operating Expenditures Per Pupil	2003 Residential Assessment Per Pupil	Current Funding Model	New Funding Model G
Beautiful Plains	7,151	58,160	59%	85%
Border Land	7,689	53,012	57%	83%
Brandon	6,646	87,126	56%	81%
D.S.F.M.	9,282	77,393	51%	70%
Evergreen	7,888	141,906	51%	77%
Flin Flon	7,356	67,393	56%	71%
Fort La Bosse	8,077	48,011	53%	84%
Frontier	12,341	19,611	43%	45%
Garden Valley	6,164	56,702	66%	87%
Hanover	5,760	55,846	67%	86%
Interlake	7,317	72,135	61%	83%
Kelsey	7,350	46,395	68%	88%
Lakeshore	7,566	48,543	69%	87%
Lord Selkirk	7,460	114,980	57%	79%
Louis Riel	7,360	96,285	54%	77%
Mountain View	8,051	64,136	60%	81%
Mystery Lake	8,196	53,155	66%	83%
Park West	8,156	43,779	57%	87%
Pembina Trails	7,911	125,776	44%	69%
Pine Creek	7,808	39,124	63%	91%
Portage La Prairie	7,138	65,795	58%	81%
Prairie Rose	7,816	64,793	56%	83%
Prairie Spirit	8,544	38,321	61%	92%
Red River Valley	7,982	58,325	57%	85%
River East Transcona	7,083	89,618	58%	79%
Rolling River	7,796	65,800	55%	79%
Seine River	7,821	68,412	64%	84%
Seven Oaks	7,585	89,163	55%	75%
Southwest Horizon	8,349	48,106	54%	87%
St. James-Assiniboia	7,294	101,793	47%	72%
Sunrise	8,166	95,202	53%	74%
Swan Valley	8,163	55,116	61%	83%
Turtle Mountain	7,431	57,772	58%	84%
Turtle River	8,412	44,757	71%	90%
Western	7,094	71,954	57%	79%
Winnipeg	8,265	65,533	50%	80%
Provincial Total	**7,893**	**78,744**	**54%**	**77%**

Table 9

2003 Special Levy Mill Rates

	Current * Funding Model	New ** Funding Model G	Change Mills	%
Beautiful Plains	17.7	14.3	(3.4)	-19.3%
Border Land	21.1	11.9	(9.2)	-43.8%
Brandon	17.6	10.4	(7.2)	-40.8%
Evergreen	17.1	10.1	(7.0)	-40.7%
Flin Flon	24.2	10.7	(13.6)	-55.9%
Fort La Bosse	19.2	13.6	(5.6)*	-29.3%
Frontier	23.6	14.2	(9.4)	-39.7%
Garden Valley	18.4	10.6	(7.9)	-42.6%
Hanover	17.4	8.6	(8.8)	-50.6%
Interlake	20.5	13.8	(6.7)	-32.7%
Kelsey	23.0	9.6	(13.4)	-58.3%
Lakeshore	21.9	13.6	(8.2)	-37.7%
Lord Selkirk	20.2	10.9	(9.3)	-46.0%
Louis Riel	23.9	13.2	(10.7)	-44.6%
Mountain View	22.3	14.5	(7.8)	-35.1%
Mystery Lake	33.8	14.8	(19.1)	-56.4%
Park West	19.6	11.4	(8.3)	-42.2%
Pembina Trails	24.4	15.8	(8.6)	-35.1%
Pine Creek	21.7	14.9	(6.9)	-31.6%
Portage La Prairie	18.5	14.2	(4.4)	-23.6%
Prairie Rose	19.2	14.9	(4.3)	-22.3%
Prairie Spirit	21.9	11.1	(10.8)	-49.1%
Red River Valley	21.2	15.2	(6.1)	-28.5%
River East Transcona	24.0	13.5	(10.6)	-44.0%
Rolling River	20.7	14.9	(5.8)	-28.2%
Seine River	23.6	12.0	(11.6)	-49.2%
Seven Oaks	28.3	16.4	(11.9)	-42.1%
Southwest Horizon	20.3	16.6	(3.7)	-18.0%
St. James-Assiniboia	19.8	15.9	(3.9)	-19.8%
Sunrise	22.6	15.4	(7.2)	-31.8%
Swan Valley	23.5	13.2	(10.3)	-44.0%
Turtle Mountain	20.7	18.7	(2.1)	-9.9%
Turtle River	23.1	17.7	(5.4)	-23.3%
Western	21.4	13.2	(8.2)	-38.4%
Winnipeg	28.6	17.2	(11.4)	-39.8%
Provincial Average	**23.3**	**14.2**	**(9.0)**	**-38.6%**

Notes:

1. 2003 mill rates are derived for these divisions with differential mill rates.

Source: 2003-2004 TAXMOD4

* Mill rate applies to all property classes.

** Mill rate applies to residential property only.

Sustainability/Increased provincial funding requirements

To sustain a new education funding model and maintain an 80/20 balance between the provincial and local contributions, it will be important that school divisions contain expenditures within funding levels provided by the province and concurrently, that the provincial contribution to divisional operating budgets reflect the actual costs incurred in school divisions for program and service delivery. To the extent that there is a mismatch between these two, the system will quickly slide back to the present situation.

In jurisdictions where the provincial contribution to education is at the upper level, there has sometimes been very intense debate about the discrepancies between that which is funded and expectations and needs as seen by parents, by communities and by school authorities. At a provincial contribution of 80%, and local property taxation at 15% or lower, school divisions will have significantly less discretionary spending than is now the case. It will be critical, therefore, that the province articulate clearly that which constitutes a defined education program for Manitoba students. Moreover, provincial funding to school divisions must ensure full and complete access to a defined education program for all students wherever they may attend public school, taking into account variables such as population demographics, geographical factors and special needs incidence.

In moving to an 80% provincial contribution for public education, the issue of labour costs presents a significant challenge. With 80 to 85 percent of divisional budgets dedicated to employee salaries and benefits, cost containment in this area is essential to the sustainability of the model. Settlements determined through existing bargaining mechanisms generally reflect trends in other sectors or comparable organizations, and in the current financing arrangement, a significant portion of such settlements is funded through school division tax levies. The long term sustainability of the funding model proposed herein, hinges greatly on the on-going degree of congruency between labour costs and the level of the provincial contribution to school division operating budgets. It is clear that current processes do not achieve such congruency and the Working Group acknowledges the difficulty and the complexity in devising alternative strategies to address this issue.

Notwithstanding these considerations, it is reasonable to assume that in future years, education expenditures will continue to increase in like manner to other sector of the provincial economy. With the provincial contribution set at 80%, and assuming the province continues to increase education

funding to the rate of economic growth, annual provincial funding requirements to school division operating budgets will increase.

Table 10 illustrates two potential strategies for the future and the implications of each for sustainability of the proposed model.

Table 10

Provincial Funding Strategies and Sustainability Implications

	Year 1	%	Year 2	%	$ Change	% Change
Keep Pace Model - $ millions						
Operating Revenue	1,438		1,495		57	4%
Provincial Share	1,150	80%	1,196	80%	46	4%
School Division share	288	20%	299	20%	11	4%
Economic Growth Model - $ millions						
Operating Revenue	1,438		1,495		57	4%
Provincial Share	1,150	80%	1,173	78.5%	23	2%
School Division share	288	20%	322	21.5%	34	11.8%

In the 'Keep Pace' model the 80% provincial share is applied to a projected growth in total school division operating costs. In this example, it is assumed that if operating expenditures grow in total by 4%, then provincial funding must increase by 4% in order to maintain provincial funding at an 80% level. The economic growth model contrasts the effect of a provincial funding growth rate less than projected expenditure growth. The result is slippage in the provincial funding share and an exponential increase in the special levy share to make up the unfounded difference.

In addition, it will also be necessary to link the rate of growth to operating funding levels and treat capital funding requirements for debt servicing as an incremental amount towards ensuring that government share of operating is maintained at 80%. Presently the economic growth factor is applied to total provincial funding which includes both operating and capital (debt servicing) funding requirements. Increases in capital funding requirements come at the expense of operating funding levels, leaving a smaller effective operating funding increase that contributes to a lower provincial share. To offset this in the above examples, an additional $3.7M would be required to fund capital requirements (based on the 2004/05 funding announcement) beyond any operating funding increase.

The province would decide annually on the funding sources for the increase. If the annual funding increase were sourced entirely through general revenues, then farm and commercial property taxation would become a diminishing share of the cost of public education.

Property tax structures

Among the five principles of public education outlined by the Working Group is the notion that education is both a shared benefit to and a shared responsibility of all citizens. It is important that Manitoba's property tax structure support this fundamental principle. It is the view of the Working Group that there is merit in examining existing aspects of this structure to ensure they are consistent with the objective to achieve a greater level of shared responsibility and greater equity in the financing of our public education system.

More specifically and within this context, if property taxation is to remain an essential element of the education funding structure the Working Group then proposes the following:

- the assessment and taxation of property in provincial parks, notably residential and commercial property, in a manner consistent with other property;
- an examination of how intensive livestock operations are assessed and classified to take into account the commercial nature of the operations; and
- an examination of the homeowner's property tax credit program, including possible elimination the program and redirection of the funding to directly support education programming.

The provincial Municipal Tax Sharing program is not impacted in the proposed new funding model, nor is it in dispute. However, the 2001 AMM Task Force report entitled Rethinking Education Funding did identify reconfiguration of provincial – municipal tax sharing arrangements as one component of a multi-pronged approach to restructuring education funding in Manitoba. The Working Group encourages the Government of Manitoba to explore with municipalities the potential which may exist in this regard.

SUMMARY OF RECOMMENDATIONS

In coming to its conclusions. the Working Group sought to balance the urgent need for decreased reliance on property taxation revenues to fund public education within the scope of the challenge and the fiscal capacity of the province to act.

The Working group. therefore. recommends:

- adoption and implementation of Model G to effect
  - an increase in provincial funding support from the current 57% of divisional operating expenditures to 80%. resources to be derived from provincial general revenues and from taxation levied on farm and non-residential property classes;
  - a decrease in school division funding requirement from the current 43% to 20%. 15% to be derived from taxation levied on residential prqperty only and 5% from other revenue sources: and
  - an initial overall decrease in property taxation revenues in support of public education from 51% to 37%.

To implement the proposed funding model. the Working Group recommends:

- the pooling of farm and non-residential assessments and taxation of these property classes by the province at uniform mill rates for each;
- establishment of initial uniform mill rates for farm and non-residential property classes at the existing provincial average rate in order that the current total amount of property taxes paid by these two property classes remain unchanged in the first year of implementation;
- a 3-year self-funding phase-in period to effect the transition to uniform mill rates for farm and non-residential assessment pooling;
- a 1% increase in provincial retail sales tax to fund the increased general revenue requirement:
- legislative measures to ensure that property tax savings are passed through from landlords to tenants in rental properties:
- mechanisms to avoid erosion of initial property tax savings to home owners through subsequent increases in school division tax levies to address any mismatch between provincial funding increments and school division cost changes; and
- development of a funding distribution model which closely matches provincial funding to current actual cost factors of program and service delivery in schools.

To ensure long term sustainability of the proposed funding model, the Working Group recommends:

- articulation of a defined education program and provincial funding commensurate to ensure equity of entitlement and access for all K – S4 students in Manitoba;

- development of mechanisms to ensure on-going congruency between labour costs and the level of provincial contribution to divisional operating expenditures;

- annual adjustments to school divisions' operating funding to reflect the actual cost increases incurred in delivery of a defined education program for all students;

- separation of operating and capital funding requirements in determining provincial contribution to maintain 80% operating support;

- sourcing of annual provincial funding increases from general revenues to ensure that over time, farm and non-residential property taxation becomes a diminishing portion of the total revenue base for public education;

- review and revision of existing property taxation structures and mechanisms to address current inequities which have been identified; and

- review of provincial-municipal tax sharing arrangements with Manitoba municipalities.

CD/bu